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China, Peoples Republic of

Wine

Market Update

2003

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Report Highlights:
In 2002, China imported 2.4 million liters of American wine, thereby comprising the 14th largest market for U.S. exports by value. In the past several years, the Chinese market for imported wines has shifted from Hong Kong sourcing to direct imports (mostly via Shanghai), and from bulk to bottled wine. Although table wine is increasingly popular, consumer understanding, particularly of foreign wines, remains largely non-existent. This report describes recent developments in China's wine market; GAIN report CH3803 outlines follow-up information, including trade show and import company listings.

Includes PSD changes: No
Includes Trade Matrix: No
Unscheduled Report

Shanghai ATO [CH2], CH

I. Market Overview

China's aggregate market for imported wine has produced conflicting data; however, a few trends have become evident within the melee of developing, increasingly linked, regional markets. Shanghai's direct imports of bottled wine have increased steadily (Figure 1), while trans-shipments through Hong Kong continue to decline. Importer and distributor options for getting wine into China have also increased, both in quality and diversity. These trends combine with growing disposable income, declining import duties, and government promotion to create growth opportunities for producers willing to focus and conduct due diligence.

Over the past three years, bulk and bottled American wines have had opposite experiences in China's market. Increased domestic production has largely replaced bulk imports while lower tariffs have smoothed the way for bottled imports. Between 2000 and 2002, Chinese Customs statistics indicate that imports of American bulk wine plummeted from 908,303 liters to 313,324 liters. On the other hand, imports of bottled American wine (in containers of less than 2 liters) increased 68 percent from 262,795 liters in 2000 to 442,276 in 2002. As China continues to develop its domestic wine industry, American exporters are likely to find more comparative advantage in the bottled, middle and high range of this developing market.

Figure 1. Shanghai Bottled Wine Imports: Top Five Suppliers

Country	Millions of US $			% Share			%Change
	2000	2001	2002	2000	2001	2002	(02/01)
France	0.608	0.955	1.605	31.50	41.56	35.04	68.05
United States	**0.298**	**0.455**	**1.021**	**15.46**	**19.82**	**22.30**	**124.25**
Australia	0.170	0.265	0.716	8.81	11.54	15.65	170.19
Italy	0.417	0.195	0.350	21.63	8.50	7.63	79.11
Spain	0.055	0.171	0.254	2.88	7.44	5.54	48.45
World	**1.929**	**2.298**	**4.579**	**100**	**100**	**100**	**99.31**

Source: China Customs

The quantity and quality of domestic wine production has steadily increased over the past five years. In 1998, demand exceeded China's domestic production of 220 million liters. The shortfall in domestic production brought about an infusion of foreign bulk wine for local blending and bottling, with the result that most Chinese label wines contained 30-40 percent imported bulk wine. Infusions of largely European viticulture technology and expertise in the form of joint ventures have helped domestic companies eliminate the production shortfall. Dubious media reports of foreign 'garbage wine' being blended with Chinese wine have helped to further reduce the sales of foreign bulk wine and make way for new Chinese production. Growth in domestic wine production helps explain the shrinkage of the overall wine import market as indicated by Chinese Customs statistics over the past three years.

Figure 2. China's Total Wine Imports (including bulk, bottled, and sparkling wines)

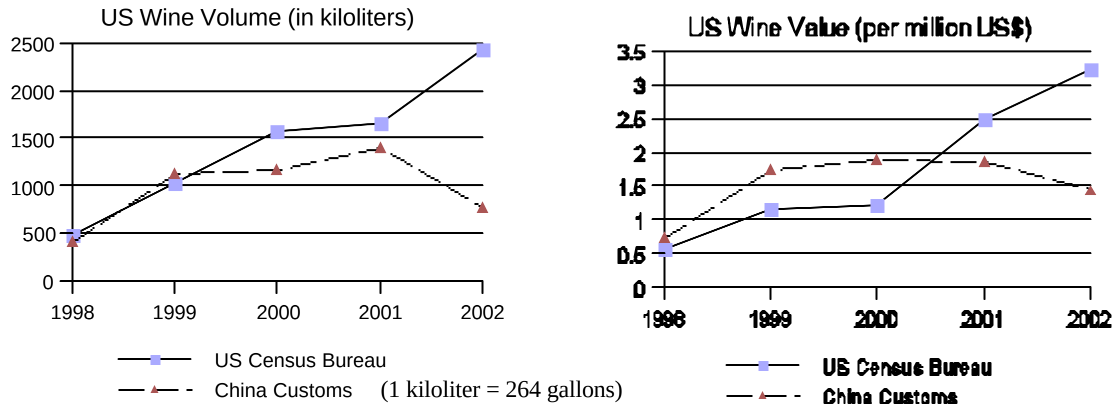
Country	Millions of US $			% Share			% Change
	2000	2001	2002	2000	2001	2002	(02/01)
Chile	1.988	6.063	9.296	7.03	25.69	39.90	53.33
France	4.843	5.310	5.016	17.13	22.50	21.53	-5.55
Argentina	0.185	0.509	1.663	0.66	2.16	7.14	226.58
Australia	0.702	0.834	1.635	2.48	3.53	7.02	96.18
Italy	4.441	3.357	1.577	15.71	14.23	6.77	-53.02
United States (#6)	**1.908**	**1.883**	**1.440**	**6.75**	**7.98**	**6.18**	**-23.56**
Spain	13.485	5.027	1.403	47.70	21.30	6.02	-72.09
Germany	0.275	0.181	0.391	0.97	0.77	1.68	115.22
World Total	**28.272**	**23.601**	**23.297**	**100**	**100**	**100**	**-1.29**

Source: China Customs

The overall decline in value for four of the eight countries listed in Figure 2 illustrates the difficulty and instability of China's market for imported wines. Not only do many Chinese prefer sweet wine, but imports are too expensive for the vast majority of Chinese consumers. Once wines do successfully enter the Chinese market, food service and consumer education levels are extremely low, not to mention the lack of proper storage facilities. Although it is large and dynamic, it is not uncommon for invested foreign producers to miss China's market entirely.

Just as Figure 1 and Figure 2 indicate contrasting pictures of China's imported wine market, Chinese and American statistics differ on the size and development of the aggregate market. Whereas US export statistics show continued growth in the volume and value of American wine exports to China, Chinese Customs data indicate a contraction of imports (Figure 3). Beyond issues of methodology and reporting, this disparity illustrates the need for American producers to focus their distribution and marketing on specific, accessible market niches.

Figure 3. Data Disparities for American Wine in China



II. Domestic Wine Industry

China's grape-growing area expanded 40 percent between 1997 and 2002, and growth is expected to maintain an average annual rate of 12 percent through 2007. In 2002, it was estimated that 186,670 hectares of land in China were planted with grapes, with an average annual yield of 3.5 million tons. The top wine producing provinces are Hebei, Shandong (northern coastal provinces) and Xinjiang (China's westernmost province). According to SOPEXA, France's food industry organization, national wine output grew 30 percent over between 1997 and 2002, and is predicted to expand 15 percent per year through 2007.

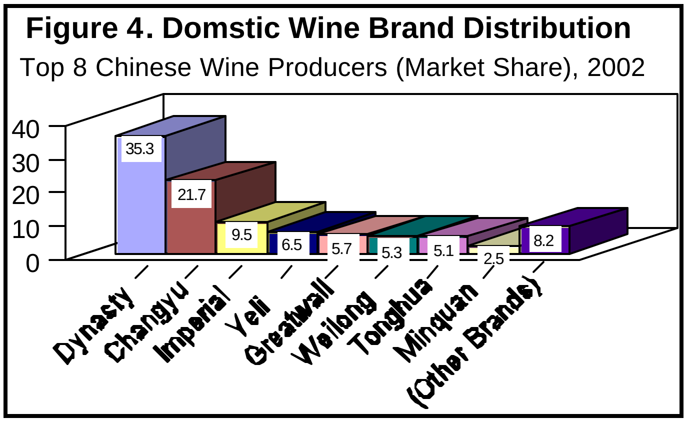


Figure 4. Domstic Wine Brand Distribution

Source: Business Information of Shanghai, 2002 FMCG Guide

As China moves to increase wine production capacity, it is also seeking to improve product quality. In September 2002, China agreed to join the Office International de la Vigne et du Vin (O.I.V). The OIV is an intergovernmental organization based in Paris which is concerned with scientific and technical aspects of wine. Two months after joining the OIV, China's State Economic and Trade Commission released a new set of National Technical Specifications for Vinification– a further regulatory evolution of the domestic wine industry.

Increased regulation corresponds to a gradual shift in consumption away from traditional sweet wines, such as muscatel (*meikui lujiu*) and Osmanthus (*guihua jiu*), and grain alcohol (*bai jiu*), to dry grape wines. Many domestic wine companies have created hybrid products to address this transition. In retail markets for example, bottles of Chinese Cabernet are sometimes wrapped with packing tape that attaches a smoothing bottle of Coke or Sprite. Likewise, Great Wall sometimes offers complementary bottles of lemonade, while a mint-flavored white wine from Sichuan province advertises itself as "refreshing with ice water".

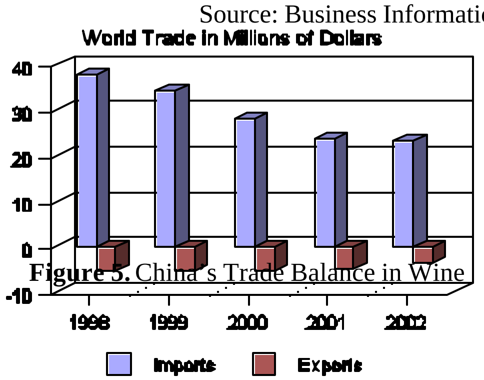
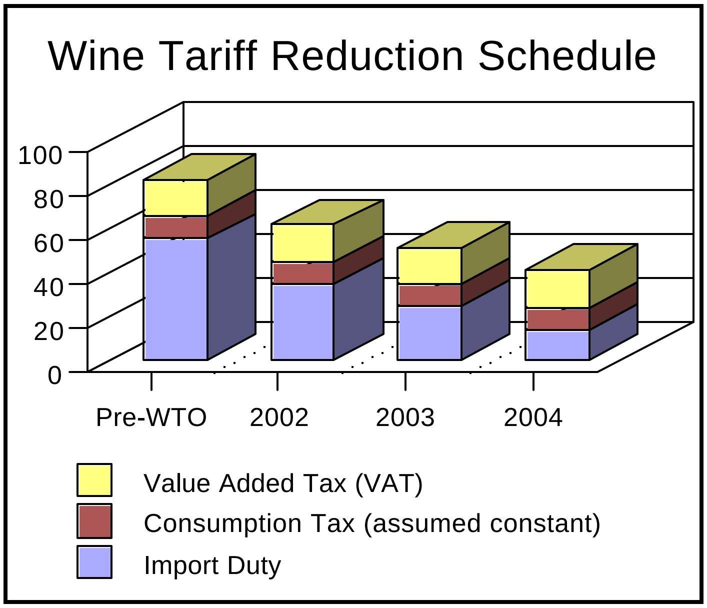


Figure 5. China's Trade Balance in Wine

Recent increases in production and regulation of China's wine industry have not been matched by increased exports. In fact, China's wine exports have steadily declined from 4.2 million liters in 2000, to 3.03 in 2001, and 2.35 in 2002, according to China Customs data. The crunch of expanded production, declining exports, and increased foreign competition accounts for the extensive and unconventional marketing of domestic wines to fill just about every imaginable market niche.

III. Import Information



According to WTO accession agreements, import duties on American wine will decline from a 2002 level of 34.4% to 24.2% in 2003, and 14% in 2004. However, in the event that foreign wines gain market share, many importers expect that consumption taxes will be increased to offset lower duties. Importers may also wish to note that the formula for calculating total tax results in a rate that is more than the sum of its parts.

(All rates are ad valorem assessed on a CIF basis.)

Import Customs Duties (ICD): 24.2%
Value Added Tax (VAT): 17%
Consumption Tax (CT): 10%

Total import tax will be ICD+CT+VAT, to be calculated in the following formula:

$$\text{Total Tax} = \frac{\text{ICD Rate} + \text{CT Rate} + \text{VAT Rate} + (\text{ICD Rate} \times \text{VAT Rate})}{1 - \text{CT Rate}}$$

$$= \frac{24.2\% + 10\% + 17\% + (24.2\% \times 17\%)}{1 - 10\%} = 61.5\%$$

In 2004, the ICD Rate is scheduled to be reduced to 14%, which will result in a total tax of 48.2% (assuming a constant CT Rate). The 2003 ICD for bulk wine is 29%, which results in a total tax of 67.7%; the bulk wine ICD will drop to 20% in 2004.

The Chinese food labeling law was designed and promulgated by the State Bureau of Technical Supervision to apply to all pre-packaged food and beverage products to be marketed in China including alcoholic beverages, and closely follows standards recommended by the FAO and World Health Organization's CAC (CODEX STAN 1-1991). The law only applies to labels on "delivery units" that are pre-packaged for retail sales (i.e., bottled wine), but does not affect "shipping units" and bulk goods. After the promulgation of the old food labeling law which went into effect for Chinese-produced pre-packaged foods on February 1, 1995, the law was revised in a span of less than one year, and finally resulted in an extension specifically granted to imported pre-packaged foods. A new law was put into effect on September 1, 1996, which also appeared to discourage the use of temporary adhesive labels (Chinese language stickers). Nevertheless, most foreign wines in China have continued to use their original label in the front with a Chinese language sticker attached to the back of the bottle. Customs and quarantine officials made it known that they would enforce the labeling law more stringently for new products entering China after March 1, 2003; however, this has not resulted in any drastic new enforcement measures. For the foreseeable future, adhesive labels are likely to remain acceptable for bottled wine as long as the Chinese portion is at least as large as the original language portion. In the long run, producers are advised to develop compliant Chinese labeling for eventual full enforcement. Moreover, voluntary Chinese labeling may serve U.S. producers in complementing promotion efforts and clearly differentiating their products from low-end copycat products and blatant imitations.

For further information, reports CH3804, CH1043, and CH1044 cover Enforcement, the Food Labeling Standard, and Food Labeling Management Regulation, respectively.
Whether they are printed on original packaging or on a sticker, labels for imported wines, champagne, sparkling wines, and sake should include the following contents in Chinese:

1. Name or Brand of the Wine
2. Ingredients
3. Net Content (ml)
4. Alcoholic Content (%) (V/V)
5. Production Date (yy/mm/dd)
6. Packer / Distributor / Importer (Name & Address)
7. Content of Must (%) (Sake is exempted from this requirement)
8. Country of Origin
9. Quality Guarantee and/or Storage Period (yy/mm/dd)
10. Content of Sugar (gram/l)

In addition to packing list and other standard documents, wine exports to China require official-looking certificates of origin and health. Since FDA and USDA do not produce such certificates for wine exports, bottling companies and wineries often produce a 'Certificate of Analysis' which is then paired with an official-looking, sealed, 'U.S. Certificate of Origin' from the local chamber of commerce. Some competitor country governments do produce export certificates, however the winery and chamber of commerce certificates are sufficient to pass Customs.

IV. Importer / Distributors in the Domestic Market

Traditionally, wine entered the market via three channels, namely:

- China National Cereals, Oils & Foodstuffs Import and Export Corporation (CEROILS), the state monopoly wholesaler and distributor of alcoholic beverages.
- Joint Venture and Foreign-owned hotels, as well as duty free stores under China Travel Services (CTS); generally a limited channel as products are restricted from general distribution.
- The 'Grey Channel' of Hong Kong and Guangzhou; this route is closing with the decline of direct import duties and more stringent enforcement of import regulations.

The current method for most successful importer/distributors is to obtain a sub-license from CEROILS and then to handle the marketing and distribution themselves. The integrated importer-distributor arrangement usually provides more control over brand development, proper handling, and storage compared to the state-owned distribution option. At present, a few foreign-owned and managed top wine importer/distributors engage in every aspect of sales and marketing, including climate-controlled warehousing, trade education, market promotion, sales, and delivery. As the dominant port of entry for American wine (Figure 6), Shanghai offers several foreign-run, fully integrated, import and distribution options. The problem with these full service import options is that they are in high demand and therefore reluctant to add new products whose success is not a sure thing.

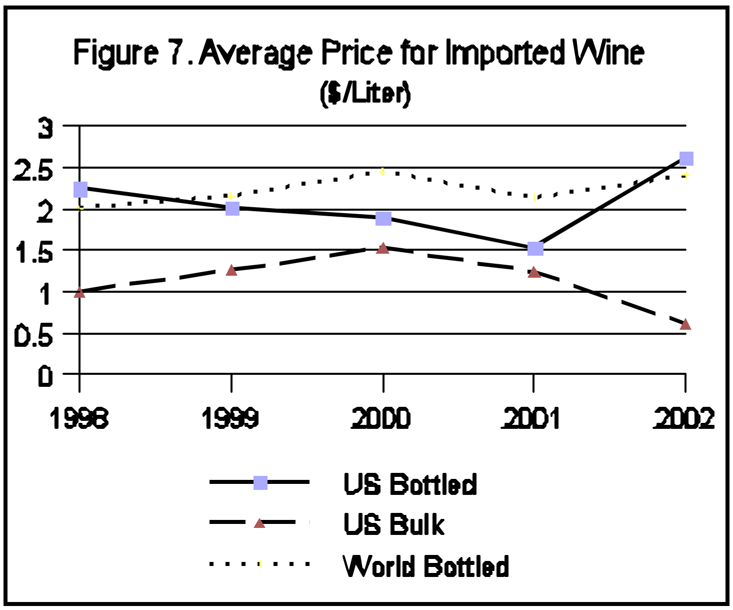
Figure 6. China's Top Five Ports for Bottled American Wine (by total value; in containers of less than two liters)

Port	Millions of US $			% Share			% Change
	2000	2001	2002	2000	2001	2002	02/01
Shanghai	**0.298**	**0.455**	**1.021**	**60.09**	**80.32**	**88.02**	**124.25**
Tianjin	0.072	0.047	0.069	14.45	8.29	5.94	46.60
Shenzhen	0.030	0.035	0.036	6.10	6.14	3.07	2.44
Guangzhou	0.035	0.002	0.025	7.06	.032	2.18	1219.86
Beijing	0.023	0.016	0.009	4.59	2.85	0.73	-47.43
All Ports	**0.496**	**0.567**	**1.160**	**100**	**100**	**100**	**104.63**

Source: China Customs

Media reports on the health benefits of red wine have stimulated increased urban retail sales. Nonetheless, two thirds of the wine consumed in China is still purchased in hotels and restaurants, according to the market research firm Access Asia. For producers targeting retail and food service, the best way to learn about the Chinese market and meet distributors/clients is to participate in industry promotions and trade shows. A list of relevant trade shows and importing companies is available in GAIN report CH3803. A complimentary list of ATO-organized promotions is available in CH2826: the ATO Promotional Opportunities Report.

Within the spectrum of options, it is most important for producers to have a good relationship with their importer/distributor to ensure that the entire supply process is adequately administered all the way to the consumer. Many Chinese importer/distributors, particularly those who may be interested in sourcing a new, untested American wine, have not developed marketing and education services to accompany their distribution services. Unless they are competitively priced or comprehensively introduced through educational promotions, new products often fail to earn a sustainable market niche, even in relatively developed coastal markets. Beyond the pre-formed market of business travelers and expatriates, it is essential to conduct extensive marketing and educational activities to develop a critical cohort of Chinese consumers.



Source: China Customs

Aside from education and marketing, the most influential factor in the success or failure of selling foreign wines in China is pricing. Figure 7 illustrates the recent rise of average bottled wine prices as more high-end American producers have entered the market. In Shanghai, the target price point for a 750 ml bottle of foreign wine hovers around 55 RMB (about $7), compared to the 35 RMB price point for domestic dry red wine.

The convergence of declining import duties and sustained economic growth has created a variety of timely opportunities for American producers to enter China's more developed markets. Producers who identify a market niche and establish a solid relationship with their importer/distributor are most likely to succeed in marketing their product. As the Beijing government encourages the ongoing transition from grain alcohol to more healthy and agriculturally efficient wine consumption, producers may wish to remember Homer’s account of wine in the Odyssey: "Wine can of their wits the wise beguile, make the sage frolic, and the serious smile."

V. Additional Information

For additional information about exporting to China, please refer to the ATO Shanghai web page (http://www.atoshanghai.org) and download a copy of the **Exporter Guide** and **Business Travel in China**. For up-to-date information about labeling laws and importation regulations, please see the **FAIRS** report (also available on the ATO website). For additional information about marketing California wines in China, contact the Wine Institute of California:

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Shanghai Imported Food Enterprise Association (SIFEA) – An industry association representing food import companies; their services include facilitating the food label inspection process.

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